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No. 78-1384

In the Supreme Court of the United States

OCTOBER TERM, 1978

HENRY A. PROESEL and LA SALLE NATIONAL BANK, ET AL., PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

WADE H. MCCREE, JR.
Solicitor General
Department of Justice
Washington, D.C. 20530

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The sole question presented in this federal estate tax case is whether an estate is permitted an estate tax deduction under Section 2053(a)(3) of the Internal Revenue Code of 1954 (26 U.S.C.) with respect to gift taxes and interest paid pursuant to a "split gift" election made by the executor under Section 2513 of the Code and Treasury Regulations thereunder.

The pertinent facts are as follows: The decedent, Frieda Proesel, died on August 12, 1965 (Pet. App. 2). During 1964, decedent's husband made taxable gifts of real property valued at $429,137.68 (Pet. App. 2). Because of an extension of time granted by the Internal Revenue Service, he did not file a federal gift tax return for this period until January 3, 1966, several months after his wife's death (Pet. App. 2). At that

time, he filed his own individual gift tax return and, in his capacity as executor of his wife's estate, a gift tax return on behalf of the estate, electing "split gift" treatment of the gifts under Section 2513 of the Code (Pet. App. 2-3). The estate then sought to deduct the gift taxes and interest paid by it pursuant to this "split gift" election as a claim against the estate under Section 2053(a)(3) (Pet. App. 3-4). On audit, the Commissioner of Internal Revenue disallowed the deduction on the ground that the gift taxes and interest in question were not personal obligations of the decedent at the time of her death (Pet. App. 4). In this refund suit brought by the estate in the United States District Court for the Northern District of Illinois, the district court upheld the Commissioner's position that the gift taxes were not deductible by the estate as claims against the estate for estate tax purposes because the decedent had no enforceable obligation to pay such taxes at the time of her death. The court of appeals affirmed (Pet. App. 1-13).

1. The courts below correctly held that the gift taxes and interest were not deductible as claims against the estate under Section 2053(a)(3) of the Code. The pertinent Treasury Regulations expressly provide that the only claims deductible under Section 2053(a)(3) are those which "represent personal obligations of the decedent existing at the time of his death, whether or not then matured, and interest thereon which had accrued at the time of death." Treasury Regulations on Estate Tax, Section 20.2053-4 (26 C.F.R.). As the court of appeals observed (Pet. App. 6-7), petitioners do not challenge the validity of this Regulation, which was first promulgated 60 years ago under the provisions of the Revenue Act of 1918, ch. 18, 40 Stat. 1057,[1] and approved by this Court in *United States* v.

[1]See Treasury Regulations 37 (1919 ed.), Art. 45.

Stapf, 375 U.S. 118, 132 (1963). Thus, for purposes of this case, the controlling fact is that at the time of her death, the decedent had not assumed personal liability for any portion of the gift taxes imposed by the Code with respect to the gifts made by her husband in 1964.

Section 2513 was enacted in order to reduce the impact of the difference between the gift tax imposed in the case of gifts of community property and the tax imposed on transfers of property owned by one spouse or the other in common law states. See H.R. Rep. No. 1274, 80th Cong., 2d Sess. 24-26 (1948); S. Rep. No. 1013, 80th Cong., 2d Sess. 26-28 (1948). The statute permits spouses to elect to treat a gift made by either of them as a "split gift," *i.e.*, one-half made by the husband and one-half by the wife, thereby reducing the overall rate of the gift tax. The "split gift" provisions, however, apply only where both spouses consent to the election in the manner prescribed by the pertinent Treasury Regulations under Section 2513(a)(2) and (b). The Regulations provide that such consent to elect split gift treatment must be made on gift tax returns filed by the husband or wife (or both), and that the executor or administrator of a deceased spouse may give the requisite consent. Treasury Regulations on Gift Tax, Section 25.2513-2(a)(1) and (c) (26 C.F.R.). Here, the decedent's husband gave such consent to split gift treatment on the gift tax return in his capacity as her executor. But the critical fact for purposes of this case, involving the deductibility of the taxes as a claim against the estate, is that the decedent did not personally consent to the gift tax liability prior to her death. Since an enforceable claim against her estate did not arise until the gift tax return was filed on January 3, 1966, the taxes are not deductible as a claim that existed at the time of death.

2. Without specifically challenging the validity of Section 20.2053-4 of the Treasury Regulations, or the correctness of the lower courts' ruling that decedent herself had not, at the time of her death, assumed personal liability for the gift taxes here in question, petitioners argue (Pet. 5) that the decision below unconstitutionally discriminates between residents of community property states and those in common law property states. But it has long been recognized that gifts of community property, or income from community property, would not be subject to tax on the same basis as gifts of, or income from, property owned by individual spouses in common law jurisdictions. While Congress has sought to minimize these differences as they affect federal estate, gift and income taxes, it has never been thought that it was compelled to do so as a matter of constitutional precept, or that a statutory scheme which does not achieve a perfect equality between the residents of community property states and the residents of non-community property states would be subject to constitutional defect. As this Court recently observed in a similar context in *San Antonio School District* v. *Rodriguez*, 411 U.S. 1, 41 (1973): "No scheme of taxation, whether the tax is imposed on property, income, or purchases of goods and services, has yet been devised which is free from all discriminatory impact." See also *Brushaber* v. *Union Pacific R.R.*, 240 U.S. 1, 24-25 (1916); *Steward Machine Co.* v. *Davis*, 301 U.S. 548, 583-584 (1937).

3. Petitioners further argue (Pet. 5) that the decision below violates the intent of Congress in enacting the split gift provision. But the legislative history accompanying the enactment of Section 2513 shows that Congress specifically "recognized that complete equalization of the estate and gift taxes cannot be achieved because of the inherent differences between

community property and noncommunity property." S. Rep. No. 1013, *supra*, at 27. Moreover, as the court of appeals pointed out (Pet. App. 8-9), the fact is that decedent's husband and her estate fully enjoyed the specific benefit Congress intended to confer under these "split gift" provisions—*i.e.*, "to have the gift treated [for gift tax purposes] as though each had made one-half of the gift." H.R. Rep. No. 1274, *supra*, at 26.

Jones v. *Commissioner*, 327 F. 2d 98 (4th Cir. 1964), upon which petitioners rely (Pet. 6-7), is not to the contrary. There, the court held that although the taxpayer's wife had not signed the "Consent of Spouse" form attached to the gift tax return, the return sufficiently manifested the wife's consent to the split gift because she had signed the consent form on prior returns. Here, on the other hand, no gift tax returns signifying either spouse's consent in any fashion had been filed prior to the decedent's death. At best, she had merely expressed an intention (which she remained free to disavow at any time) eventually to consent to the application of these provisions. Thus, at the time of the decedent's death, she was not subject to personal liability for these gift taxes. They were accordingly not a deductible claim against the estate.[2]

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[2]The question presented in this case has been eliminated by Section 2001(a)(5) and (d)(1) of the Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1848, 1854. The new legislation added Section 2035(c) to the Code, which effectively denies an estate the benefit of a deduction as a result of the payment of federal gift taxes on any gift made within three years of the decedent's death.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

WADE H. MCCREE, JR.
Solicitor General

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